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90454—36

In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 330

THE UNITED STATES, PETITIONER

v.

AUTOMATIC WASHER COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the Court of Claims in the above entitled cause.

OPINION BELOW

The opinion of the Court of Claims is reported in 15 F. Supp. 70.

JURISDICTION

The judgment of the Court of Claims was entered on June 1, 1936. The jurisdiction of this Court is invoked under Section 3(b) of the Act of February 13, 1925.

QUESTION PRESENTED

Stockholders of a corporation who were entitled, pursuant to a reorganization plan, to shares in a new corporation, agreed that certain of such shares should be delivered by the new corporation to a nominee of the stockholders, who was authorized to sell such shares for the account of the stockholders and to designate the names in which the stock certificates should be issued. Did this transaction involve a transfer by the stockholders to their nominee of a right to receive shares of stock, within the stamp tax provisions of the Revenue Act of 1926?

STATUTE AND REGULATIONS INVOLVED

The pertinent portions of the Revenue Act of 1926 and regulations thereunder will be found in the Appendix, *infra,* pp. 12–14.

STATEMENT

The special findings of fact of the Court of Claims may be summarized as follows:

Respondent, hereinafter referred to as the "new company", is a Delaware corporation, engaged in the business of manufacturing electric washing machines. Its predecessor, as owner of that business, was Automatic Electric Washer Company, an Iowa corporation, hereinafter referred to as the "old company" (Fdg. 1).

On June 22, 1928, one Nelson, a stockholder and officer of the old company, entered into an agreement with Folds, Buck and Company, hereinafter

referred to as the "Bankers", which provided that Nelson would bring about a reorganization of the old company, to be accomplished by the organization of a new corporation under the laws of Delaware, which would acquire all the assets of the old company; that the capital structure of the new corporation should consist of 180,000 shares of common stock, of which 40,000 shares were to be retained in the treasury, and 40,000 shares of convertible preference stock, both without par value; that upon such reorganization the Bankers should have the option and privilege of purchasing 40,000 shares of preference stock and 40,000 shares of common stock of the new company (Fdg. 2).

The new company was thereupon organized, and on or about September 27, 1928, entered into an agreement with the old company, which provided that the old company would convey all its assets to the new company, which would assume the liabilities of the old; and, as consideration for such conveyance, the new company would deliver to the stockholders of the old company 34,538 shares of convertible preference stock and 140,000 shares of common stock of the new company; that the stockholders of the old company, as had been agreed among themselves, would contribute the shares of convertible preference stock and a pro rata proportion of common stock received by each of them to make up the total of 34,538 shares of convertible preference stock and 40,000 shares of common stock which were to be sold to the Bankers; that

in order to carry out said sale each of the stockholders of the old company irrevocably appointed Nelson and one Gallagher attorneys in fact to receive the stock of the new company to which such stockholder might be entitled, and to make the sale thereof to the Bankers, distributing the proceeds of such sale pro rata to the stockholders of the old company; that accordingly the new company should issue certificates of its stock as ordered by Nelson and Gallagher to the amount of 34,538 shares of preference and 40,000 of common, which shares were to be delivered to Nelson and Gallagher for sale to the Bankers (Fdg. 3).

The powers of attorney theretofore executed by all the stockholders of the old company provided in part that Nelson and Gallagher were appointed attorneys for such stockholders; that said attorneys were authorized to receive the shares of stock of the new company accruing to such stockholders, and to sell such stock in consummating the agreement with the Bankers; and that said power of attorney was to remain in full force and effect until November 15, 1928, and should not be subject to revocation (Fdg. 4).

Under these agreements, on or about October 1, 1928, the old company transferred to the new company all assets and properties subject to all of its liabilities, and the new company thereupon issued 140,000 shares of its common stock and 34,538 shares of its convertible preference stock, delivered as follows: 100,000 shares of common to the in-

dividual stockholders of the old company in proportion to their holdings in the old company; 40,000 shares of common to Nelson (of which 7,069 shares were Nelson's pro rata portion, as a stockholder of the old company, of the new common stock to be sold to the Bankers); and 34,538 shares of convertible preference to Nelson (of which 6,104 shares were Nelson's pro rata portion, as a stockholder of the old company, of the preference stock to be sold to the Bankers) (Fdg. 5). Nelson thereupon sold and transferred to the Bankers 40,000 shares of common and 34,538 shares of preference stock, collecting the proceeds thereof and distributing the same among the stockholders of the old company (Fdg. 6).

The respondent duly paid the stamp tax imposed by the Revenue Act of 1926 on the original issue of 140,000 shares of common and 34,538 shares of preference stock. It also paid the stamp tax on the subsequent transfer by Nelson to the Bankers of the 40,000 shares of common and 34,538 shares of preference stock (Fdg. 7).

Thereafter the Commissioner of Internal Revenue demanded and collected from respondent two additional stamp taxes on the foregoing transactions, one of $4,020.46 on the transfer by the old company to its stockholders of the right to receive from the new company 140,000 shares of common and 34,538 shares of preference stock, and one of $1,593.63, including interest and penalty, on the transfer by the stockholders of the old company to

Nelson of their rights to receive the 40,000 shares of common and 34,538 shares of preference stock ultimately sold to the Bankers (Fdg. 8).

The validity of the tax of $4,020.46 on the transfer by the old company to its stockholders of the right to receive the stock of the new company was conceded by respondent in the court below, and the claim on this item was abandoned (Fdg. 9).

Respondent, on or about June 12, 1931, filed claim for refund in the amount of $1,593.63, representing the tax on the transfer by the old stockholders to Nelson. This claim was rejected by the Commissioner of Internal Revenue on or about November 10, 1931 (Fdg. 10).

Suit was brought in the Court of Claims on October 14, 1933, and on June 1, 1936, judgment was entered for the plaintiff in the amount of $1,593.63, with interest.

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that the transfer by the stockholders of the old company to their nominee of their right to receive stock in the new company was not subject to the stamp tax imposed by the Revenue Act of 1926.

2. In failing to hold that the transfer to Nelson of the stock ultimately sold to the Bankers was a taxable transfer under the statute.

3. In holding that respondent was entitled to recover $1,593.63, with interest, and entering judgment for respondent in said amount.

4. In failing to enter judgment for the United States and dismissing the petition.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Founders General Corporation* v. *Hoey,* decided July 6, 1936, not yet officially reported, but found in 1936 Prentice Hall, Volume I, Par. 1378. In that case the taxpayer corporation subscribed to shares in another corporation and directed that they be issued in the name of Benton & Co. as the taxpayer's nominee. Benton & Co. was a partnership whose sole business was to take and hold in its name securities belonging to the taxpayer. Neither the partnership nor any of its members had any interest in securities so held. The contract between the taxpayer and the partnership provided that the latter was appointed agent

> for the limited purpose of holding in the firm name * * * securities and property as agent (other than commission agent or broker) for the account of the Corporation and of otherwise acting with respect thereto in accordance, but only in accordance with the written instructions of the Corporation * * * *.

It was also provided that the partnership should have no "beneficial interest" in securities so held, and that it waived all right, title, and interest in any security held or received by it. The Court of

Appeals in that case held that the taxpayer corporation had transferred to its nominee the right to receive shares for which it subscribed, and that the imposition of a stamp tax in respect of that transfer was, under the statute, "inevitable."

The only substantial differences in the facts of that case and the case at bar serve to strengthen the conclusion that the Commissioner's determination in the present case was correct. In the *Founders General* case the securities were never actually delivered to the nominee, but were received by the taxpayer corporation itself. This circumstance was held not sufficient to defeat the tax, since the taxpayer corporation, by directing that the shares be issued in the name of its nominee, had transferred to the nominee the right to receive the shares. In the present case no such circumstance exists; not only the right to receive but actual receipt vested in the nominee. A second difference in the two cases is that, so far as appears in the *Founders General* case, the designation of the nominee and the powers vested in it were completely revocable; in the present case, on the other hand, the powers granted to the nominee were made irrevocable for a fixed period of time (Fdg. 4).

2. The decision below fails to apply the principles announced by this Court at the last Term in *Raybestos Manhattan Co.* v. *United States,* 296 U. S. 60. In holding the stamp tax provisions to be applicable in the circumstances there disclosed, this Court said (p. 64):

> Here the power to command the disposition of the shares included the right to receive them and the exercise of the power which transferred the right is subject to the tax.

It cannot be disputed that in the case at bar the power to command the disposition of the shares was in the stockholders. The right to receive the shares could be vested in others only by transfer from the stockholders themselves. This was fully recognized in the agreement between the old and the new corporations. That agreement recited that the stockholders agreed to "contribute" certain shares to be sold to the Bankers; that the "stockholders of the Old Company will sell and deliver to the said Bankers" the shares in question; and that Nelson and Gallagher had been appointed attorneys in fact "to receive the respective securities of the New Company to which such stockholder may be entitled" (Fdg. 3). It is, of course, immaterial that the stockholders did not receive the shares with respect to which they transferred rights to their nominee. In the *Raybestos Manhattan* case, *supra,* the old corporation was held to be a transferor where the securities were issued directly by the new corporation to the shareholders of the old.

As was said in the *Raybestos Manhattan* case, "The subject of the tax is not alone the transfer of ownership in shares of stock. It embraces transfers of rights to subscribe for or receive shares or

certificates, * * *" (p. 63). This conclusion, under which the transaction in the present case is subject to the tax, is clearly compelled by the language of the statute. Section 800–A (3) provides for a tax on all "transfers of legal title to shares or certificates of stock * * * or to rights to subscribe for or to receive such shares or certificates * * *." The regulations, *infra*, p. 14, provide (Article 34 (u)):

> Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock.

In holding the transaction in the present case to be non-taxable, the court below has in effect enlarged the class of exemptions provided in the statute.

3. The importance of the question presented is indicated by the frequency of litigation involving stamp taxes upon transfers by corporations to their nominees of the right to receive and dispose of stock. A decision in accord with that of the court below was rendered by the Circuit Court of Appeals for the Seventh Circuit on June 30, 1936, in *A. B. Leach & Co., Inc.*, v. *United States*, not yet officially reported but found in 1936 Prentice Hall, Vol. 1, par. 1362. The Government is petitioning for certiorari in the *Leach* case (No. 331, Present Term). The decision of the court below is also in accord with *Union Trust Co.* v. *Heiner*, 26 F. (2d) 391 (W. D. Pa.). The *Union Trust Co.* case was specifically disapproved by the Circuit Court of

Appeals for the Second Circuit in the *Founders General* case, *supra,* Judge A. N. Hand stating—

> It is plain that the court in *Union Trust Co.* v. *Heiner* ignored the express provision that the absence of any beneficial interest on the part of the holder should not exempt the transfer from taxation. The decision, therefore, proceeded on an indefensible theory. That decision has since been followed by various district courts, but we cannot avoid the conclusion that it is contrary to the plain meaning of the statute.[1]

The question involved herein will continue to arise, since the 1932 Revenue Act, section 723, continues the same provisions. Because of the importance of the question and the conflict of decisions in the lower courts, the application of the stamp tax provisions to transfers involving nominees without beneficial interest should be authoritatively settled by this Court.

Wherefore it is respectfully submitted that this petition for writ of certiorari should be granted.

STANLEY REED,
Solicitor General.

SEPTEMBER 1936.

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[1] *Union Trust Co.* v. *Heiner* was followed in *Dean* v. *Caldwell & Co.*, 9 F. Supp. 177 (M. D. Tenn.), and *National Bond & Share Corp.* v. *Hoey*, 14 Fed. Supp. 787 (S. D. N. Y.). The latter decision can no longer be regarded as authoritative, in view of the decision of the Circuit Court of Appeals in the *Founders General* case.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 800. On and after the expiration of thirty days after the enactment of this Act there shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in Schedule A of this title, * * * the several taxes specified in such schedule. * * * (U. S. C., Title 26, Secs. 900, 908).

SCHEDULE A.—STAMP TAXES

* * * * *

2. *Capital stock, issue.*—On each original issue, whether on organization or reorganization, of certificates of stock, or of profits, or of interest in property or accumulations, by any corporation, on each $100 of face value or fraction thereof, 5 cents: *Provided,* That where a certificate is issued without face value, the tax shall be 5 cents per share, unless the actual value is in excess of $100 per share, in which case the tax shall be 5 cents on each $100 of actual value or fraction thereof, or unless the actual value is less than $100 per share, in which case the tax shall be 1 cent on each $20 of actual value or fraction thereof.

The stamps representing the tax imposed by this subdivision shall be attached to the stock books and not to the certificates issued.

3. *Capital stock, sales or transfers.*—On all sales, or agreements to sell, or memo-

randa of sales or deliveries of, or transfers of legal title to shares or certificates of stock or of profits or of interest in property or accumulations in any corporation, or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not, on each $100 of face value or fraction thereof, 2 cents, and where such shares are without par or face value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share: * * * (U. S. C., Title 26, Sec. 901).

Treasury Regulations 71:

ART. 31. *Basis of tax.*—Every transfer or sale of stock, either before or after issuance of a certificate, is taxable. The tax accrues at time of making the sale or agreement to sell or memorandum of sale, or delivery of, or transfer of the legal title to shares, or certificates of stock, or of profits, or of interest in property or accumulations in any corporation, joint-stock company, or association, or of the right to subscribe for or to receive such shares or certificates, regardless of the time or manner of the delivery of the certificate or agreement or memorandum of sale.

ART. 34. *Sales and transfers subject to tax.*—The following transactions are subject to the tax:

(a) The sale, or transfer, or change of ownership, of certificates of stock, or of profits, or of interest in property or accumu-

lations in corporations, joint-stock companies, or associations.

(b) The sale or transfer of shares of stock, whether or not represented by certificates.

(c) The transfer of stock to or by trustees.

* * * * *

(g) The transfer of the interest of a subscriber for stock, however such interest may be evidenced or conditioned upon further payments.

(h) The transfer of the right to subscribe for stock in any corporation, joint-stock company, or association, whether or not evidenced by warrants.

* * * * *

(t) The transfer of the right to receive stock which a corporation has unconditionally agreed to issue.

(u) Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock.

U. S. GOVERNMENT PRINTING OFFICE: 1936